



**AUDIT COMMITTEE  
KIVA CONFERENCE ROOM  
3939 NORTH DRINKWATER BLVD.  
CITY OF SCOTTSDALE  
SCOTTSDALE, AZ 85251**

**MONDAY, APRIL 21, 2008**

**PRESENT:** Jim Lane, Committee Chairman  
Wayne Ecton, Committee Member  
Ron McCullagh, Committee Member

**ALSO PRESENT:** Cheryl Dreska, Office of City Auditor  
Joyce Gilbride, Office of City Auditor  
Lisa Gurtler, Office of City Auditor  
Kim Prendergast, Office of City Auditor  
Ellie Kim, Office of City Auditor  
Susan English, Office of City Auditor  
Richard Chess, Financial Services  
Michelle Korf, The Downtown Group  
Jim Green, Cultural Council  
John Cocca, Police Department  
Paul Nowinski, Police Department  
Bill Moloney, Police Department  
Brent Stockwell, Community Services  
Connie James, Community Services  
Debra Baird, Community Services

**CALL TO ORDER/ROLL CALL**

Chairman Lane called the Audit Committee meeting to order at 2:03 p.m. Roll call was taken confirming the presence of the Committee Members.

**MINUTES - Approval of March 27, 2008, Committee Meeting Minutes**

Committee Member Ecton made a motion to approve the March 27, 2008, minutes. Committee Member McCullagh seconded the motion. The minutes were approved by a unanimous vote of three (3) to zero (0)

## **GENERAL BUSINESS**

### **Agenda Item 1      Discussion on draft report - Controls Over the Safeguarding, Use, and Disposal of Seized and Forfeited Property, and Funds Advanced to the Police Department for Undercover Operations Report No. 0704.**

Assistant City Auditor Lisa Gurtler presented the Committee with Audit Report No. 0704, and introduced Assistant Police Chief John Cocca and Asset Forfeiture Detective Bill Moloney, who were instrumental in this audit.

Ms. Gurtler explained that the two fundamental components of this audit were asset seizure and forfeiture, and an audit of two imprest checking accounts that deal with the day-to-day operations of special investigation funding.

There was approximately \$4 million in cash generated as a result of asset forfeitures. These funds are held by the Maricopa County Attorney or the State Attorney General's Office, and transferred to the City based on a quarterly application submitted by the asset forfeiture detective. The audit revealed that the police department does comply with state, county, and federal requirements and the assets are properly safeguarded.

Ms. Gurtler said opportunities for improvement were identified including the segregation of duties, the tagging of assets converted to City use valued over \$5,000, and timely submission of required reports and reimbursement requests. In addition, the audit revealed certain transactions that can be eliminated.

In regard to the imprest checking accounts, the audit revealed the assets are safeguarded and handling of the funds complies with policy and procedures. Opportunities for improvement include adherence to those operation orders and development of a process to monitor the timeliness of the court deposits.

In regard to tagging assets valued at over \$5,000, Committee Member McCullagh asked how those items are valued. Ms. Gurtler stated the value is determined based on the discretion of the Asset Forfeiture Detective. Asset Forfeiture Detective Bill Moloney explained that all items put into use at the police department are monitored and tracked in an internal database, and thus far there has only been one item above \$5,000 requiring tagging. Committee Member Ecton said that was a City financial policy, and he did not feel \$5,000 was an unreasonable amount. Chairman Lane asked if the tagged items are within a control group separate from other items. Assistant Chief Cocca said they are all in a control group; however, a specific tag will be placed on items valued at \$5,000 or more.

City Auditor Cheryl Dreska explained the police department will be working on setting values in conjunction with the Purchasing Department. Chief Cocca said the Department is now having the item itself viewed and valued by the warehouse before it goes into service.

Chairman Lane expressed concern that this is a potentially significant internal control issue. He said the amount of assets noted in the report would be worthy of at least a supervisory signoff, and perhaps an occasional review of what transactions are taking place.

Ms. Gurtler explained there are controls in place that include supervisory approval, but there is one common person throughout the whole process.

Chairman Lane asked if there are any recommendations from the Audit Department that would potentially divide up the functions within this department. He indicated a crossover function would be beneficial to ensure compliance. Ms. Gurtler said the police department is currently in the process of cross training another employee in this area to assist. Chief Cocca indicated this person would be an assistant in the event the primary Asset Forfeiture Detective became unavailable. Chairman Lane said that would not necessarily address this issue of separating the functions within the department of receiving and maintaining assets, and selling and disposing of them.

Committee Member Ecton said although nothing has occurred to cause concern, he would like to see this system improved.

Chairman Lane explained if there are not control features in place, events could potentially not be recorded resulting in never finding an exception. Ms. Gurtler said the audit tested this by obtaining independent records from various agencies to ensure there were no irregularities. Chief Cocca stated there is a paper trail on each item starting from the moment it is confiscated.

In response to a question from Chairman Lane, Chief Cocca indicated there are situations where this merchandise is returned. Chairman Lane said that would serve as an independent check.

Committee Member McCullagh asked for clarification regarding how the property is sold after the process is complete. Chief Cocca said the police department has used Sierra Auctions for a number of years to sell the items, and explained in detail how that process works.

Chairman Lane said re-involving Fleet Management with the disposal of vehicles would be worthy of consideration, as long as fund control can be maintained.

Ms. Dreska said her main concern is the lack of training for an Asset Forfeiture Detective replacement, should Detective Moloney be unable to carry out his duties. She said with the commitment from the police department regarding bringing in the warehouse and Fleet Management for valuations, she is comfortable with the current process.

In response to a question regarding Item No. 4 from Chairman Lane, Chief Cocca indicated there is a post-approval process if pre-approval is not possible. He noted the audit revealed additional documentation is necessary regarding what the monies are spent on. Those deficiencies have already been corrected and the new policies are in the process of going through the Policy Review Committee and the Legal Department. While the sergeant does a monthly review of the expenditures from the imprest accounts, more detail is necessary for documentation purposes.

Chairman Lane asked for additional clarification regarding the flow of money from items sold at auction. Chief Cocca explained while it would be more efficient to let the auction house handle the exchange of money directly with the County, Sierra Auctions is not as

automated as the police department would like them to be and there is concern regarding getting the proper documentation back to the department.

Due to the volume of items and funds flowing through this department, Chief Cocca requested these audits be performed more frequently.

Ms. Dreska stated this document would not come back to the Committee; however, Committee Members will receive a copy of the final report

**Agenda Item 2      Discussion on draft report - Housing Assistance and CDBG Programs Report No. 0614**

Senior Auditor Kim Prendergast stated fieldwork for this audit was completed in December of 2007. The programs reviewed included Section 8 housing, housing rehabilitation, and payments to public service activities. In general, the internal controls in the Community Assistance Office are sufficient and the staff is well trained on applicable regulations.

Two areas for improvement were identified within the Housing Rehabilitation Program. The first involves tracking change orders. According to current guidelines, homeowners are not responsible for change orders on housing rehabilitation projects unless they exceed the maximum loan amount allowed under the program. In 10 of 17 housing rehabilitation projects, the promissory note was less than the outlay to rehabilitate the home.

The second area of improvement involves monitoring contractor progress for potential liquidated damages. According to the current guidelines, contractors are to be penalized \$50 for each calendar day that work remains unfinished. There was not sufficient documentation to determine if liquidated damages should have been assessed.

Staff has agreed with the areas for improvement, and Ms. Prendergast identified management's responses on page two of the CDBG report.

Committee Member Ecton asked if the problem was with the documentation itself, or not enough time and staff to do the proper documentation. In regard to Item 1, Acting Community Services General Manager Brent Stockwell explained that the program guidelines and contracts do not currently authorize the updating or re-recording of lien documents for those cases. In order to do that, the procedures and the contracts would require revision. In regard to Item 2, the documentation was provided in the file, but it was not integrated in with the change orders. Staff is researching that item to incorporate it in the future.

Chairman Lane asked if federal funds were at risk in regard to Item 1. Mr. Stockwell said the City is leveraging federal funds that could be granted and instead doing a deferred loan program and recapturing those funds for reuse. He explained that there are cases where the change order amount would not warrant re-recording a lien. Ms. Dreska explained the program potentially loses federal funds when change orders are not updated; however, the Audit Department is not advocating re-recording liens in all instances. A process that modifies the promissory note between the City and the homeowner is suggested.

Committee Member McCullagh asked how many of these home improvement loans are granted in a given year. Mr. Stockwell indicated there were 17 granted in Fiscal Year (FY) 06/07. The average amount of each loan was approximately \$19,941.

In response to a question by Committee Member McCullagh, Mr. Stockwell explained he is not aware of a situation where the project cost less than the lien amount. Since the City is acting as the bank in these cases, Committee Member McCullagh proposed writing the note for the maximum amount and adjusting the loan at the end of the project. Committee Member Ecton said that this proposed solution might be met with reluctance on the part of homeowners. Mr. Stockwell said all options will be explored with Financial Services and the City Attorney's Office.

The Committee accepted draft Audit Report No. 0614 as presented.

**Agenda Item 3          Discussion on draft report - Management Services Agreement  
Scottsdale Mall Report No. 0510C.2.**

Ms. Dreska explained this audit deals with the services of the Mall coordinator and issuing permits on the Mall. Much of this section deals with the City's government liquor license, which is used to provide alcohol on certain portions of the Mall.

Ms. Dreska stated the audit has revealed that the government liquor license is not currently in the City's name, an agent has not been appointed, nor has an on-site manager been appointed, as is now required under statutory law. A Series 5 liquor license can only be issued to the government. In addition, auditors could not find an approved premise boundary for the City's government liquor license.

Ms. Dreska indicated the alcohol beverage concessionaire agreement that was entered into in 1993 between the City and the Cultural Council will expire July 1, 2008, if not extended. That agreement sets out the Cultural Council's use of the City's liquor license. The Cultural Council has subcontracted with another vendor to do those services. While the City Attorney's Office believes the concession agreement allows them to subcontract, there is a concern that the arrangement does not protect the City's interests. In addition, it does not provide that the net revenues go back into the management of the arts facility, which was the initial intent of obtaining the government liquor license.

While the application process for a special event liquor license is administratively processed, the applications are signed by the Mayor without Council approval. Under state law, the governing body must either approve special event liquor licenses, or designate an individual to act on its behalf in that regard.

There is currently no process in place to deal with the removal of solid waste from the Mall. The Solid Waste Division helped facilitate the Cultural Council in obtaining 30 residential roll-off containers, which are filled and then rolled to the curb where they are picked up as part of the residential trash collection process. The Cultural Council was not billed for that service until July of 2007. The Solid Waste Management Division implemented an "artificial rate," and then back charged the Cultural Council to January 2007. Overtime staff handles solid waste that occurs in excess of what can be handled by the roll offs. Those overtime hours are tracked and the Cultural Council bills the

event and repays the City for that charge. The City absorbs the overtime associated with solid waste removal from the Arts Festival.

Ms. Dreska explained the last issues deal with charging fees for use of the Mall. By ordinance, the fees are set by the City Council. Those fees have not been reviewed since they were last updated. The Cultural Council has been charging fees for permits that are not in line with what the Council approved, and have identified different areas for the Mall than what the City Council set out in the fee schedule.

Chairman Lane asked who sets the fee schedules on those permits. Ms. Dreska stated under the terms of the Management Services Agreement, the Cultural Council can retain all permit fees in repayment for all of the activities they perform as the Mall coordinator. However, the City sets the fee amounts under the current structure.

Committee Member Ecton said one issue is in the way the contract was written and managed. In addition, there are issues the City needs to correct going forward. In the City's attempt to get a cultural program started 20 years ago, sufficient controls were not established for managing it.

Chairman Lane asked whether the corrective measures required by the City are still tied to the administration of an unclear contract. Ms. Dreska said three things will need to happen simultaneously in order to correct these issues: Completion of the Management Services Agreement, an evaluation and modification of City Code that deals with the Scottsdale Mall, and the alcoholic beverage concession agreement and licensing. In addition, the City Council will need to make policy decisions on the special event liquor licenses, liquor license premise boundaries, and the appointment of an agent.

Aside from the liquor license issues, Chairman Lane said many of these items have been addressed in the new Management Services Agreement and are in the process of being corrected. Michelle Korf from the Downtown Group stated all items of concern will either be addressed in the new Management Services Agreement or in the update of the Scottsdale Mall ordinance.

Chairman Lane asked for clarification regarding the one "disagree" noted in the report. Ms. Dreska clarified it is related to the name of the Mall. City Code sets out the name of the mall as Scottsdale Mall; however, none of the documentation reviewed during the audit referred to it by its proper name.

Chairman Lane asked if any of the items of concern caused a loss of funds to the City. Ms. Dreska said while that is difficult to determine, there are costs that the City absorbed that were not anticipated or addressed when this structure was initially crafted in the early 1990's.

The Committee accepted draft Audit Report No. 0510C.2 as presented.

**Agenda Item 4      Update by the City Auditor on status of current projects.**

Assistant City Auditor Joyce Gilbride introduced the newest member of the Audit Division, Ellie Kim.

Ms. Dreska distributed an outline for the Committee to follow, and explained the first four items are carryover audits that are currently being finalized. The WestWorld Financial Audit is currently in for review with a plan to have a draft report delivered to management next week.

The Scottsdale Cares Audit is currently the only report with no findings, and has been provided to management for review.

The Audit of Use of Outside Counsel has been completed. The report is in draft with a plan to get it to the City Attorney for review this week.

The General Provisions for the Management Services Agreement report is through internal review; however, auditors have a follow-up question for the City Attorney's Office before it is distributed to management.

The remaining items are from the current plan that the Committee approved. Fieldwork is underway for the Use of the Basin Management Funds Audit. A draft report will be issued on or before May 30, 2008.

The Collection of Development and Permit Fees Audit has been rescheduled due to placing staff on the Fact-Finding Report requested by Council. An initial interview with the department has been conducted, but the preliminary survey will not begin until the middle of May with a draft report issued on or before June 30th.

The preliminary survey on the Efforts to Manage Costs Associated with Workers' Compensation Claims Audit preliminary survey will be completed by May 1, 2008. A risk matrix will be discussed with staff this week.

Staff has met with surrounding municipalities to discuss the steps they take to control their fire department assets. The preliminary survey for the Audit of Fire Department Assets is to be completed by May 1, 2008. Chairman Lane asked what assets this audit will be looking at. Ms. Dreska explained this audit will encompass everything except the rolling stock and facilities. The Fleet Division and Municipal Services track the rolling stock and CPM tracks the facilities, so these were eliminated from the scope of the audit.

The estimate for the Fact-Finding Report is May 31, 2008, depending upon access to the City Clerk and City Attorney's information.

The last audit to be completed is the Code Enforcement follow up, which has been postponed. More information regarding that follow up will be available by the end of May.

Committee Member McCullagh expressed concern that the list provided to the Committee is difficult to follow since it does not show what the original audit plan was, and does not include a list of audits not being worked on. Ms. Dreska indicated at the next meeting she will include the audit plan that was approved for the fourth quarter and present the Committee with the status of those audits. The only audit not on the list that was scheduled for the fourth quarter is the Code Enforcement Audit, which was postponed when the Fact-Finding Report was added by City Council.

Ms. Dreska indicated if there is concern regarding the decision to delay the Code Enforcement Audit, that discussion could be agendaized for the next Committee meeting.

**PUBLIC COMMENTS - None**

**COMMITTEE COMMENTS - None**

**ADJOURNMENT**

With no further business to discuss, the Audit Committee meeting adjourned at 3:30 p.m.